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SUBJECT: BRAZILIAN BANK MERGER CREATES LARGEST IN SOUTHERN
HEMISPHERE

SENSITIVE BUT UNCLASSIFIED--PLEASE PROTECT ACCORDINGLY

¶1. (U) Unibanco and Itau announced the merger of their two Brazilian banking institutions on November 3. The combined bank, Itau Unibanco Holding SA, will become the largest private financial institution in the Southern Hemisphere and among the top 20 banks worldwide. Itau was previously the third largest Brazilian bank, while Unibanco was the fifth largest. Itau's news release noted that the negotiations had been ongoing for 15 months; however, the financial crisis likely precipitated the merger. Though the merger still requires the approval from the Brazilian Central Bank (BCB) and the two companies' boards of directors, it is the first within the Brazilian financial sector in the wake of the global financial crisis. Initial investor reaction on Brazil's stock exchange was positive with both companies' stock climbing double digits, and analysts said the deal shows a return of confidence to the sector. Finance Minister Guido Mantega said the merger should help improve liquidity within the Brazilian banking system.

¶2. (U) According to Economatrica, the new institution will be the sixth largest in market value globally among all U.S. and Latin American banks, ahead of Merrill Lynch and Goldman Sachs. The total market value of the two institutions is approximately USD 274 billion. Together, they will have 14.5 million clients with checking accounts and 4,800 banks, both representing approximately 18 percent of the market. They will jointly manage 19 percent of the credit volume and 21 percent of deposits.

¶3. (SBU) For Unibanco, the merger offers an opportunity to recover from the impact that AIG's U.S. losses had on the company. AIG had been an integral part of Unibanco's insurance arm. (Note: In 1997, AIG bought 50 percent of equity in Unibanco's insurance division. End Note.) Unibanco had been the biggest player by far for large corporate insurance policies and had about 30 percent market share in the Brazilian insurance business. Unibanco also held shares in several other companies, including the Brazilian Reinsurance Institute (IRB), which was a recently privatized bank that had held a monopoly on reinsurance in Brazil. The BCB's Director for Economic Policy Mario Mesquita told the U.S. Treasury Attache that Unibanco wanted the merger because of an internal concern about who would take over the company after Pedro Moreira Salles retired.

¶4. (U) Itau had in turn been connected to derivatives contracts that have hit many Brazilian firms. As the larger bank, many view

the merger as more of a take-over by Itau than a traditional merger.

Indeed, Itau's CEO, Roberto Setubal will become the new head of Itau Unibanco Holding SA.

15. (SBU) Comment: The merger represents the first major corporate banking fusion since the financial crisis hit the Brazilian financial sector. The Brazilian banking sector was already extremely concentrated and further concentration, especially among Brazil's small and medium banks, is expected. Under normal circumstances, investors might have rejected the merger; however, in today's uncertain global financial climate they are likely to welcome any action that strengthens institutions. That being said, the merger could mean significant layoffs and unions are likely to be unhappy. End Comment.

16. (U) This cable was coordinated/cleared by Embassy Brasilia and the U.S. Treasury Attache in Sao Paulo.

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